

# SETTLEMENT AGREEMENT

## I. PARTIES

This Settlement Agreement ("Agreement") is entered into among the United States of America, acting through the United States Department of Justice and on behalf of the Office of Inspector General ("OIG-HHS") of the Department of Health and Human Services ("HHS") (collectively the "United States"); and HealthSouth Corporation ("HealthSouth") (hereafter referred to as "the Parties"), through their authorized representatives.

## II. PREAMBLE

As a preamble to this Agreement, the Parties agree to the following:

A. HealthSouth is a corporation organized under the laws of the State of Delaware with its headquarters in Birmingham, Alabama. HealthSouth currently provides inpatient rehabilitation health care services in 94 facilities throughout the United States.

B. The United States contends that HealthSouth submitted or caused to be submitted claims for payment to the Medicare Program ("Medicare") and the Medicaid Program ("Medicaid"), Titles XVIII and XIX of the Social Security Act, 42 U.S.C. §§ 1395-1395hhh, and 42 U.S.C. §§1396-1396v, respectively.

C. Covered Conduct. The conduct described in this paragraph shall be referred to as the "Covered Conduct." The United States contends that it has certain civil claims, as specified in Article III, Paragraph 2 against HealthSouth for submitting claims from May 1, 1988 to April 30, 2005 to Medicare and Medicaid for items and services referred by physicians: (1) with whom HealthSouth (or its agent, Medistar) had financial relationships that violated the physician self-referral law, known as the "Stark" law, 42 U.S.C. § 1395nn et seq., and/or (2) with whom

HealthSouth (or its agent, Medistar) had remunerative arrangements that violated the Anti-Kickback Statute, 42 U.S.C. § 1320a-7b(b); such financial relationships and/or remunerative arrangements are described in the following three self-disclosure reports submitted by HealthSouth to the United States: (1) Report on HealthSouth's Relationships with the Alabama Sports Medicine and Orthopedic Center, the American Sports Medicine Institute and Certain Affiliated Physicians dated October 8, 2004 (attached hereto as Exhibit 1); (2) Report on HealthSouth's Relationship with Medistar and Affiliated Physicians dated October 8, 2004 (attached hereto as Exhibit 2); and (3) Report on the Kerlan-Jobe Orthopaedic Clinic dated April 13, 2005 (attached hereto as Exhibit 3). The scope of the Covered Conduct is limited to civil claims of the United States that are predicated upon underlying violations of the Stark Law and/or Anti-Kickback Statute.

**D.** The United States contends also that it has certain administrative claims against HealthSouth for engaging in the Covered Conduct, as specified in Article III, Paragraph 3, below.

**E.** This Agreement is neither an admission of liability by HealthSouth nor a concession by the United States that its claims are not well founded. HealthSouth denies the allegations of the United States.

**F.** To avoid the delay, uncertainty, inconvenience, and expense of protracted litigation of the above claims, the Parties reach a full and final settlement pursuant to the Terms and Conditions below.

### III. TERMS AND CONDITIONS

#### A. Payment.

1. Settlement Amount. HealthSouth agrees to pay to the United States \$14,200,000 plus accrued simple interest from September 1, 2007, at an annual rate of 4.75% (the "Settlement Amount").

2. Installment payments. HealthSouth agrees to pay the Settlement Amount to the United States in two installment payments. The first installment payment in the amount of \$7,100,000 plus accrued simple interest from September 1, 2007 to the date of the payment shall be made no later than five days from the Effective Date of this Agreement. The second installment payment for the remaining balance plus accrued simple interest shall be paid on or before March 31, 2008.

3. Electronic Funds Transfer. All payments made by HealthSouth to the United States will be made by electronic funds transfer pursuant to written instructions to be provided by the United States.

4. No Prepayment Penalty. The entire balance of the Settlement Amount, or any portion thereof, due to the United States under this Agreement, may be prepaid without penalty.

B. Release of HealthSouth by the United States. Subject to the exceptions in Paragraph 4, below, in consideration of the obligations of HealthSouth set forth in this Agreement, and conditioned upon HealthSouth's full payment of the Settlement Amount, the United States (on behalf of itself, its officers, agents, agencies, and departments) agrees to release HealthSouth from any civil or administrative monetary claim the United States has or

may have under the False Claims Act, 31 U.S.C. §§ 3729-3733; the Civil Monetary Penalties Law, 42 U.S.C. § 1320a-7a; the Stark Law, 42 U.S.C. § 1395nn(g)(3); the Program Fraud Civil Remedies Act, 31 U.S.C. §§ 3801-3812; or the common law theories of payment by mistake, unjust enrichment, and fraud, for the Covered Conduct. No individuals are released by this Agreement.

C. Release of HealthSouth by HHS-OIG. In consideration of the obligations of HealthSouth set forth in this Agreement and the Second Addendum to the January 2005 Corporate Integrity Agreement (CIA) entered into between OIG-HHS and HealthSouth, conditioned upon HealthSouth's full payment of the Settlement Amount, the OIG-HHS agrees to release and refrain from instituting, directing, or maintaining any administrative action seeking exclusion from Medicare, Medicaid, and other Federal health care programs (as defined in 42 U.S.C. § 1320a-7b(f)) against HealthSouth under 42 U.S.C. § 1320a-7a (Civil Monetary Penalties Law) or 42 U.S.C. § 1320a-7(b)(7) (permissive exclusion for fraud, kickbacks, and other prohibited activities) for the Covered Conduct, except as reserved in Article III, Paragraph 4, below, and as reserved in this Paragraph. The OIG-HHS expressly reserves all rights to comply with any statutory obligations to exclude HealthSouth from Medicare, Medicaid, or other Federal health care programs under 42 U.S.C. § 1320a-7(a) (mandatory exclusion) based upon the Covered Conduct. Nothing in this Paragraph precludes the OIG-HHS from taking action against entities or persons, or for conduct and practices, for which claims have been reserved in Article III, Paragraph D, below.

**D. Exceptions to Releases.** Notwithstanding any term of this Agreement, specifically reserved and excluded from the scope and terms of this Agreement as to any entity or person (including HealthSouth) are the following:

1. Any civil, criminal, or administrative liability arising under Title 26, U.S. Code (Internal Revenue Code);
2. Any criminal liability;
3. Except as explicitly stated in this Agreement, any administrative liability, including mandatory exclusion from Federal health care programs;
4. Any liability to the United States (or its agencies) for any conduct other than the Covered Conduct;
5. Any liability based upon such obligations as are created by this Agreement;
6. Any liability for express or implied warranty claims or other claims for defective or deficient products or services, including quality of goods and services;
7. Any liability for personal injury or property damage or for other consequential damages arising from the Covered Conduct;
8. Any liability for failure to deliver goods or services due; and
9. Any liability of individuals, including officers and employees, and the physicians with whom HealthSouth (or its agent, Medistar) had the relationships included in the Covered Conduct.
10. Any liability of Medistar to the United States for the Covered Conduct.

E. Double Jeopardy, Excessive Fines and No Characterization for Tax Purposes.

HealthSouth waives and shall not assert any defenses HealthSouth may have to any criminal prosecution or administrative action relating to the Covered Conduct, which defenses may be based in whole or in part on a contention that, under the Double Jeopardy Clause in the Fifth Amendment of the Constitution, or under the Excessive Fines Clause in the Eighth Amendment of the Constitution, this Agreement bars a remedy sought in such criminal prosecution or administrative action. Nothing in this Paragraph or any other provision of this Agreement constitutes an agreement by the United States concerning the characterization of the Settlement Amount for purposes of the Internal Revenue laws, Title 26 of the United States Code.

F. HealthSouth's Release of the United States. HealthSouth fully and finally releases the United States, its agencies, employees, servants, and agents from any claims (including attorney's fees, costs, and expenses of every kind and however denominated) that HealthSouth has asserted, could have asserted, or may assert in the future against the United States, its agencies, employees, servants, and agents, related to the Covered Conduct and the United States' investigation and prosecution thereof.

G. Denied Claims. The Settlement Amount shall not be decreased as a result of the denial of claims for payment now being withheld from payment by any Medicare carrier or intermediary or any state payer, related to the Covered Conduct; and HealthSouth agrees not to resubmit to any Medicare carrier or intermediary or any state payer any previously denied claims related to the Covered Conduct, and agrees not to appeal any such denials of claims.

**H. Unallowable Costs.** HealthSouth agrees to the following:

1. Unallowable Costs Defined: that all costs (as defined in the Federal Acquisition Regulation, 48 C.F.R. § 31.205-47; and in Titles XVIII and XIX of the Social Security Act, 42 U.S.C. §§ 1395-1395hhh and 1396-1396v; and the regulations and official program directives promulgated thereunder) incurred by or on behalf of HealthSouth, its present or former officers, directors, employees, shareholders, and agents in connection with the following shall be “unallowable costs” on government contracts and under the Medicare Program, Medicaid Program, TRICARE Program, and Federal Employees Health Benefits Program (“FEHBP”):

- (a) the matters covered by this Agreement;
- (b) the United States’ audit and civil and criminal investigations of the matters covered by this Agreement;
- (c) HealthSouth’s investigation, defense, and corrective actions undertaken in response to the United States’ audits and civil and criminal investigations in connection with the matters covered by this Agreement (including attorney’s fees);
- (d) the negotiation and performance of this Agreement;
- (e) the payment HealthSouth makes to the United States pursuant to this Agreement, including any costs and attorneys fees; and
- (f) the negotiation of, and obligations undertaken pursuant to the January 2005 CIA and the October 2006 and Second (2007)

Addenda (collectively, “the CIA”) thereto to:

- (i) retain an independent review organization to perform annual reviews as described in Section III of the CIA; and
- (ii) prepare and submit reports to the OIG-HHS. However, nothing in this paragraph that may apply to the obligations undertaken pursuant to the CIA (or either Addenda) affects the status of costs that are not allowable based on any other authority applicable to HealthSouth. (All costs described or set forth in this paragraph are hereafter “unallowable costs.”)

2. Future Treatment of Unallowable Costs: These unallowable costs shall be separately determined and accounted for in nonreimbursable cost centers by HealthSouth, and HealthSouth shall not charge such unallowable costs directly or indirectly to any contracts with the United States or any State Medicaid program, or seek payment for such unallowable costs through any cost report, cost statement, information statement, or payment request submitted by HealthSouth or any of its subsidiaries or affiliates to the Medicare, Medicaid, TRICARE, or FEHBP Programs.

3. Treatment of Unallowable Costs Previously Submitted for Payment: HealthSouth further agrees that within 90 days of the Effective Date of this Agreement it shall identify to applicable Medicare and TRICARE fiscal intermediaries, carriers, and/or contractors, and Medicaid and FEHBP fiscal agents, any unallowable costs (as defined in this Paragraph) included in payments previously sought from the United States, or any State Medicaid program, including, but not limited to, payments sought in any cost reports, cost statements, information



reports, or payment requests already submitted by HealthSouth or any of its subsidiaries or affiliates, and shall request, and agree, that such cost reports, cost statements, information reports, or payment requests, even if already settled, be adjusted to account for the effect of the inclusion of the unallowable costs. HealthSouth agrees that the United States, at a minimum, shall be entitled to recoup from HealthSouth any overpayment plus applicable interest and penalties as a result of the inclusion of such unallowable costs on previously-submitted cost reports, information reports, cost statements, or requests for payment.

Any payments due after the adjustments have been made shall be paid to the United States pursuant to the direction of the Department of Justice and/or the affected agencies. The United States reserves its rights to disagree with any calculations submitted by HealthSouth or any of its subsidiaries or affiliates on the effect of inclusion of unallowable costs (as defined in this Paragraph) on HealthSouth or any of its subsidiaries or affiliates' cost reports, cost statements, or information reports. Nothing in this Agreement shall constitute a waiver of the rights of the United States to examine or reexamine the unallowable costs described in this Paragraph.

**I. HealthSouth's Cooperation With the United States.** HealthSouth agrees to cooperate fully and truthfully with the United States' investigation of individuals and entities not released in this Agreement, for the Covered Conduct. Upon reasonable notice, HealthSouth shall encourage, and agrees not to impair the cooperation of its directors, officers, and employees, and shall use its best efforts to make available, and encourage the cooperation of former directors, officers, and employees for interviews and testimony, consistent with the rights and privileges of such individuals. HealthSouth agrees to furnish to the United States, upon reasonable request, all

nonprivileged documents and records in its possession, custody, or control relating to the Covered Conduct. HealthSouth further agrees that in its continuing cooperation with the United States' investigation of individuals and entities not released in this Agreement, for the Covered Conduct, it will abide by the terms of the May 18, 2006 letter agreement that its counsel entered into with the Office of the United States Attorney for the Northern District of Alabama, the Office of the United States Attorney for the Central District of California, and the Department of Justice, Civil Division, Commercial Litigation Branch which requires HealthSouth to provide oral briefings and written materials (including, but not limited to work product prepared by certain counsel for HealthSouth and an accounting firm that may contain or reflect attorney-client communications or attorney work product) relating to Covered Conduct.

**J. Agreement for the Benefit of Parties Only.** This Agreement is intended to be for the benefit of the Parties only. The Parties do not release any claims against any other person or entity, except to the extent provided for in Article III, Paragraph K, below.

**K. No Offsets from Beneficiaries.** HealthSouth waives and shall not seek payment for any of the health care billings covered by this Agreement from any health care beneficiaries or their parents, sponsors, legally responsible individuals, or third party payors based upon the claims defined as Covered Conduct.

**L. Financial Condition.** HealthSouth warrants that it has reviewed its financial situation and that it currently is solvent within the meaning of 11 U.S.C. §§ 547(b)(3) and 548(a)(1)(B)(ii)(I), and shall remain solvent following its payment to the United States of the Settlement Amount. Further, the Parties warrant that, in evaluating whether to execute this Agreement, they (a) have intended that the mutual promises, covenants, and obligations set forth

constitute a contemporaneous exchange for new value given to HealthSouth, within the meaning of 11 U.S.C. § 547(c)(1); and (b) conclude that these mutual promises, covenants, and obligations do, in fact, constitute such a contemporaneous exchange. Further, the Parties warrant that the mutual promises, covenants, and obligations set forth herein are intended to and do, in fact, represent a reasonably equivalent exchange of value that is not intended to hinder, delay, or defraud any entity to which HealthSouth was or became indebted, on or after the date of this transfer, all within the meaning of 11 U.S.C. § 548(a)(1).

**M. Bankruptcy.** If within 91 days of the Effective Date of this Agreement or of any payment made under this Agreement, HealthSouth commences, or a third party commences, any case, proceeding, or other action under any law relating to bankruptcy, insolvency, reorganization, or relief of debtors (a) seeking to have any order for relief of HealthSouth's debts, or seeking to adjudicate HealthSouth as bankrupt or insolvent; or (b) seeking appointment of a receiver, trustee, custodian, or other similar official for HealthSouth or for all or any substantial part of HealthSouth's assets, HealthSouth agrees as follows:

1. HealthSouth's obligations under this Agreement may not be avoided pursuant to 11 U.S.C. § 547, and HealthSouth shall not argue or otherwise take the position in any such case, proceeding, or action that:
  - a. HealthSouth's obligations under this Agreement may be avoided under 11 U.S.C. § 547;
  - b. HealthSouth was insolvent at the time this Agreement was entered into, or became insolvent as a result of the payment made to the United States; or

- c. the mutual promises, covenants, and obligations set forth in this Agreement do not constitute a contemporaneous exchange for new value given to HealthSouth.

2. If HealthSouth's obligations under this Agreement are avoided for any reason, including, but not limited to, through the exercise of a trustee's avoidance powers under the Bankruptcy Code, the United States, at its sole option, may rescind the releases in this Agreement, and bring any civil and/or administrative claim, action, or proceeding against HealthSouth for the claims that would otherwise be covered by the releases provided in Article III, Paragraphs B and C above. HealthSouth agrees that

- a. any such claims, actions, or proceedings brought by the United States (including any proceedings to exclude HealthSouth from participation in Medicare, Medicaid, or other Federal health care programs) are not subject to an "automatic stay" pursuant to 11 U.S.C. § 362(a) as a result of the action, case, or proceeding described in the first clause of this Paragraph, and HealthSouth shall not argue or otherwise contend that the United States' claims, actions, or proceedings are subject to an automatic stay;
- b. HealthSouth shall not plead, argue, or otherwise raise any defenses under the theories of statute of limitations, laches, estoppel, or similar theories, to any such civil or administrative claims, actions, or proceeding that are brought by the United States within 90 calendar days of written notification to HealthSouth that the

releases have been rescinded pursuant to Article III, Paragraphs B and C, except to the extent such defenses were available on Effective Date of this Agreement; and

- c. the United States has a valid claim against HealthSouth in the amount of \$28,400,000, and the United States may pursue its claim in the case, action, or proceeding referenced in the first clause of this Paragraph, as well as in any other case, action, or proceeding.

3. HealthSouth acknowledges that its agreements in this Paragraph are provided in exchange for valuable consideration provided in this Agreement.

N. Costs. Each Party to this Agreement shall bear its own legal and other costs incurred in connection with this matter, including the preparation and performance of this Agreement.

O. Voluntary Agreement. HealthSouth represents that this Agreement is freely and voluntarily entered into without any degree of duress or compulsion whatsoever.

P. Governing Law. This Agreement is governed by the laws of the United States. The Parties agree that the exclusive jurisdiction and venue for any dispute arising between and among the Parties under this Agreement is the United States District Court for the Northern District of Alabama, except that disputes arising under the CIA shall be resolved exclusively under the dispute resolution provisions in the CIA.

Q. Entire Agreement. This Agreement constitutes the complete agreement between the Parties. This Agreement may not be amended except by written consent of the Parties.

R. Capacity to Execute. The individuals signing this Agreement on behalf of HealthSouth represent and warrant that they are authorized by HealthSouth to execute this Agreement. The United States signatories represent that they are signing this Agreement in their official capacities and that they are authorized to execute this Agreement.

S. Counterparts. This Agreement may be executed in counterparts, each of which constitutes an original and all of which constitute one and the same Agreement.

T. Successors. This Agreement is binding on HealthSouth's successors, transferees, heirs, and assigns.

U. Disclosure of Agreement. All parties consent to the United States' disclosure of this Agreement, and information about this Agreement, to the public.

V. Effective Date. This Agreement is effective on the date of signature of the last signatory to the Agreement (Effective Date of this Agreement). Facsimiles of signatures shall constitute acceptable, binding signatures for purposes of this Agreement.

THE UNITED STATES OF AMERICA

*December 14, 2007*  
DATED: December 14, 2007

BY: *Marie V. Bonkowski*

Marie V. Bonkowski  
Senior Trial Counsel  
Commercial Litigation Branch  
Civil Division  
U.S. Department of Justice

THE UNITED STATES OF AMERICA

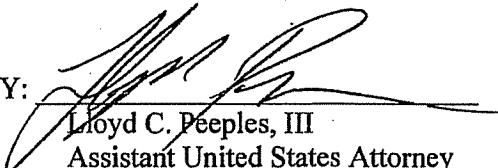
December 14, 2007  
DATED: \_\_\_\_\_

BY: Arthur S. DiDio  
Arthur S. DiDio  
Trial Attorney  
Commercial Litigation Branch  
Civil Division  
U.S. Department of Justice



THE UNITED STATES OF AMERICA

DATED: 12/14/2007

BY:   
Lloyd C. Peeples, III  
Assistant United States Attorney  
Northern District of Alabama

THE UNITED STATES OF AMERICA

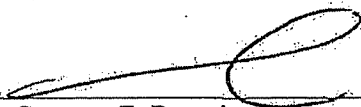
*December 14, 2007*  
DATED:                     

BY: *Wendy L. Weiss*  
Wendy L. Weiss  
Assistant United States Attorney  
Central District of California *MVB*

THE UNITED STATES OF AMERICA

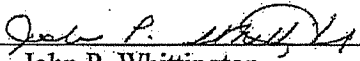
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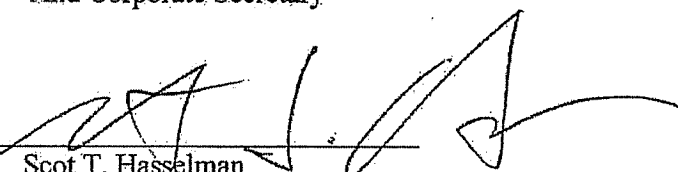
  
Gregory E. Demske  
Assistant Inspector General for  
Legal Affairs  
Office of Counsel to the  
Inspector General  
Office of Inspector General  
United States Department of  
Health and Human Services

HEALTHSOUTH CORPORATION

DATED: 12/14/07

BY:   
John P. Whittington  
Executive Vice President, General Counsel  
And Corporate Secretary

DATED: 12/14/07

BY:   
Scot T. Hasselman  
Reed Smith LLP  
Counsel for HealthSouth